

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

MANAGEMENT AND ADMINISTRATION OF
CONTRACT MDA903-91-E-0061

Report No. 97-111

March 17, 1997

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Department of Defense

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March 17, 1997

MEMORANDUM FOR ASSISTANT SECRETARY OF DEFENSE (HEALTH
AFFAIRS)
DIRECTOR, DEFENSE LOGISTICS AGENCY
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Audit Report on Management and Administration of Contract
MDA903-91-D-0061 (Report No. 97-111)

We are providing this audit report for your information and use. We performed the audit in response to concerns expressed by a complainant. We considered comments on a draft of this report in preparing the final report.

Comments on the draft of this report conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, no additional comments are required.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Ms. Mary Lu Ugone, Audit Program Director, at (703) 604-9529 (DSN 664-9529) or Mr. James Hutchinson, Audit Project Manager, at (703) 604-9530 (DSN 664-9530). Appendix D lists the distribution of this report. The audit team members are listed inside the back cover.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Management and Administration of Contract MDA903-91-D-0061

Executive Summary

Introduction. The Defense Supply Service-Washington awarded contract MDA903-91-D-0061 to the Systems Research Applications Corporation on September 18, 1991. The cost-plus-fixed-fee contract was for 1 base year with four, 1-year options and had an initial estimated value of about \$39 million. The purpose of the contract was to provide automated data processing technical support services to the DoD. As of September 17, 1996, when the contract expired, the Defense Supply Service-Washington had issued 282 delivery orders at a cost of about \$297 million.

Objective. The primary audit objective was to determine whether the Defense Supply Service-Washington and the Defense Contract Management Command managed and administered contract MDA903-91-D-0061 in compliance with the Federal Acquisition Regulation. We also evaluated management controls related to the management and administration of contract MDA903-91-D-0061. We did not review the requirements for the proposed follow-on contract because all major issues relating to that contract were resolved as reported in Inspector General, DoD, Report No. 97-001, "Award of the Sole Source Business Process Reengineering Contract," October 3, 1996. We performed both audits in response to concerns expressed by a complainant.

Audit Results. The Defense Supply Service-Washington and the Defense Contract Management Command did not fully manage and administer contract MDA903-91-D-0061 in accordance with Federal Acquisition Regulation guidance. As a result, subcontracted services were used without obtaining adequate price competition. Further, the sole-source subcontract awards were not consistently justified by the prime contractor and approved by the contracting officer, which is contrary to Federal Acquisition Regulation requirements. Also, the Defense Contract Management Command did not initiate delivery order closeout procedures until June 1996. However, the actions management initiated, as described below, will improve the Defense Supply Service-Washington contract and administration procedures on other active and future contracts.

Management Actions. The Defense Supply Service-Washington has initiated action to emphasize the importance of approved contractor purchasing systems as a control to ensure price reasonableness on large contracts with its contracting officers, has directed all contracting officers to document the approval of purchasing systems during preaward survey efforts, and will require internal review staff to verify and document all purchasing systems with the Defense Contract Management Command in all scheduled reviews over the next 6 months. Management will also send the Defense Contract Management Command the status on all delivery orders by March 17, 1997, and will give priority to completing contract modifications that extend the period of performance on active delivery orders. We consider accomplished and planned management actions appropriate and, accordingly, make no recommendations.

Management Comments. Written comments on the draft report were not required and none were received. However, Defense Supply Service-Washington managers provided oral comments. Management stated that subcontracting requests and related

consents were performed more often than reported. Management also stated that we had an insufficient basis for concluding that management control weaknesses were systemic. Management comments are further discussed in Part I.

Audit Response. We reexamined how often subcontracting requests and related consents were made and determined that the related documentation was not adequate to identify the extent of the problem. We agree that the audit's limited scope prevented a conclusion on materiality of the management control weakness, and we changed the final report accordingly.

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Part I - Audit Results

Audit Background

Contract MDA903-91-D-0061. The Defense Supply Service-Washington, an executive agency under the Department of the Army, awarded contract MDA903-91-D-0061 to the Systems Research Applications Corporation on September 18, 1991. Awarded as a cost-plus-fixed-fee contract with an initial maximum value of about \$39 million, it had a base period of 1 year with four, 1-year options. According to the contract, the contractor was to furnish the necessary personnel, materials, facilities, travel, and other services required to provide a broad range of automated data processing technical support services to the DoD.

Support services were obtained through a series of delivery orders with each delivery order priced and approved separately. As of September 17, 1996, when contract MDA903-91-D-0061 expired, a total of 282 delivery orders had been issued for technical support services and the contract value had increased to about \$297 million. As a result of concerns expressed by a complainant, we evaluated the contract's management and administration.

Contract Management and Administration. To evaluate the management and administration of contract MDA903-91-D-0061, we judgmentally selected 23 delivery orders (see Appendix B) totaling about \$123.5 million.

The Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement establish uniform policies and procedures for the acquisition of supplies and services by the DoD. Included in those policies and procedures are the roles and responsibilities of the procuring contracting officer and the administrative contracting officer.

Procuring Contracting Officer. Only contracting officers may enter into and sign contracts on behalf of the Government. Duties of the procuring contracting officer include obtaining adequate price competition; maintaining a file to document award of the contract; assigning contract administration responsibilities; and documenting all contract actions, such as modifications. For contract MDA903-91-D-0061, the contracting agency is the Defense Supply Service-Washington.

Administrative Contracting Officer. The procuring contracting officer may retain or delegate responsibility for contract administration as specified in the Federal Acquisition Regulation. For contract MDA903-91-D-0061, the Defense Supply Service-Washington delegated contract administration responsibilities to the Defense Contract Management Administration Office-Baltimore (now the Defense Contract Management Command-Baltimore). Among the responsibilities of the administrative contracting officer are:

- o reviewing, approving or disapproving, and maintaining surveillance of the contractor's purchasing system; and
- o accomplishing administrative closeout procedures.

The contract administration office maintains contract administration files until the contract is completed and evidence that all required contractual actions has been received. The administrative contracting officer then prepares a statement of contract completion, which becomes the authority for the procuring contracting officer to close the contract files.

Audit Objectives

The primary audit objective was to determine whether the Defense Supply Service-Washington and the Defense Contract Management Command managed and administered contract MDA903-91-D-0061 in compliance with the Federal Acquisition Regulation. Also, we evaluated management controls related to the management and administration of contract MDA903-91-D-0061. We did not review the requirements for the proposed follow-on contract because all major issues relating to that contract were resolved as reported in Inspector General, DoD, Report No. 97-001, "Award of the Sole Source Business Process Reengineering Contract," October 3, 1996. See Appendix A for a discussion of the audit scope and methodology, a summary of prior coverage related to the audit objectives, and our review of management controls.

Management and Administration of Contract MDA903-91-D-0061

The Defense Supply Service-Washington and the Defense Contract Management Command did not fully manage and administer contract MDA903-91-D-0061 in accordance with Federal Acquisition Regulation guidance. Contracting officials seldom provided written consent to the prime contractor for subcontracted services because they mistakenly believed the prime contractor had an approved purchasing system. As a result, subcontracted services were used without obtaining adequate price competition. Further, the sole-source subcontract awards were not consistently justified by the prime contractor and approved by the contracting officer, which is contrary to Federal Acquisition Regulation requirements. However, the Defense Supply Service-Washington has initiated responsive actions to emphasize subcontracting management requirements and, if appropriate, to strengthen contract management procedures. The Defense Contract Management Command did not initiate delivery order closeout procedures because it lost administrative oversight of the contract until June 1996. However, both organizations have initiated responsive action to close out completed delivery orders.

Subcontracting Management

We found little evidence in the contract files that the Defense Supply Service-Washington required that subcontractors be selected through competitive procedures or be otherwise justified, even though the contract contained the "Competition in Subcontracting" clause. That clause requires all subcontracts to be competed to the maximum extent practicable. Additionally, the prime contractor, Systems Research Applications Corporation, did not provide any evidence that subcontracts were routinely competed or that sole-source acquisitions were justified and approved in accordance with the Federal Acquisition Regulation. Our analysis of invoices for delivery orders in our sample showed that the Systems Research Applications Corporation subcontracted about \$50.8 million in services, or about 42 percent of the services billed.

Consent to Subcontract. In FY 1991, Federal Acquisition Regulation, subpart 44.302, required a contractor purchasing system review for each contractor whose sales to the Government, using other than sealed bid procedures, were expected to exceed \$10 million during the next 12 months. If a contractor does not have an approved purchasing system, the Federal Acquisition Regulation, subpart 44.201-2(b), states that the contractor must obtain "consent to subcontract" on all cost-reimbursement subcontracts that exceed either \$25,000 or 5 percent of the total estimated cost of the prime contract.

The Federal Acquisition Regulation defines "consent to subcontract" as the contracting officer's written consent for the prime contractor to enter into a particular subcontract. The contract files contained consent forms signed by the procuring contracting officer for few of the 116 contract actions (see Appendix B) analyzed during the audit.

Justification of Sole-source Subcontracting. The Federal Acquisition Regulation requires that considerations by the procuring contracting officer be particularly careful and thorough when subcontracts are proposed on a sole-source basis. Before providing consent, the contracting officer must consider whether:

- o the selection of the particular supplies, equipment, or services is technically justified;
- o adequate price competition was obtained or its absence was properly justified;
- o the contractor adequately assessed and disposed of subcontractors' alternative proposals, if offered;
- o the contractor has a sound basis for selecting and determining the responsibility of the particular subcontractor; and
- o the contractor performed adequate cost or price analysis or price comparisons and obtained accurate, complete, and current cost or pricing data, including any required certifications.

The contract files did not contain documentation showing that the required considerations were made by the contracting officer for the Systems Applications Research Corporation delivery orders involving subcontracts. The procuring contracting officer stated that formal consideration and specific consent was not usually made because the contractor's purchasing system had been reviewed and approved. The audit determined, however, that a review of the contractor's purchasing system had not been performed. In July 1996, more than 4 years after the contract award to Systems Applications Research Corporation, the administrative contracting officer requested a review of the Systems Applications Research Corporation purchasing system. We could not determine the specific reason for the delay in requesting a review of the purchasing system. However, at the time of initial contract award, the estimated value of the contract was not expected to exceed regulatory thresholds for purchasing system review in any year of the life of the contract.

The Defense Supply Service-Washington contract management procedures were not fully effective because the procuring contracting officer, believing the contractor had an approved purchasing system, seldom consented to contractor proposals to subcontract. Therefore, the contracting officer did not obtain subcontracted services with adequate price competition. The sole-source award subcontracts were not properly justified or approved as required by the Federal Acquisition Regulation.

Contract Administration

Contract Closeout Procedures. One function of the contract administration office is to accomplish administrative closeout procedures as specified in the Federal Acquisition Regulation. However, those procedures cannot be initiated until the contract administration office receives evidence of physical completion of the contract. For contract MDA903-91-D-0061, evidence of contract physical completion requires verification that each delivery order is completed.

Verification of Contract Deliverables. The Defense Supply Service-Washington did not verify that program officials received contracted products and services in a consistent and timely manner or that contractor performance periods were adequate for the amount of work remaining to be performed. As a result, the Defense Contract Management Command was not notified when contracted products and services were received or when performance periods were extended.

The Defense Contract Management Command did not initiate action to verify receipt of contracted products and services on contract MDA903-91-D-0061 until June 1996, more than 4 years after the contract was awarded. Management attributed the delay to staffing reductions and office relocations. On June 10, 1996, the Defense Contract Management Command requested that the contracting officer, the Defense Supply Service-Washington, verify receipt of products and services on 170 delivery orders with expired periods of performance. Subsequently, in September 1996, the Defense Contract Management Command asked the Defense Supply Service-Washington to provide certificates of acceptance on any delivery order identified in the June 10, 1996, request that had not been extended. As of November 1, 1996, the Defense Contract Management Command had identified 168 delivery orders on contract MDA903-91-D-0061 with expired periods of performance.

Management Actions

On July 17, 1996, the Administrative Contracting Officer asked the Defense Contract Management Command-Philadelphia to conduct a contractor purchasing system review for Systems Research Applications Corporation. On July 23, 1996, the Defense Contract Management Command-Philadelphia forwarded a preliminary questionnaire to the contractor for completion by August 23, 1996. The Systems Research Applications Corporation requested and received approval for an extension until January 31, 1997. The Defense Contract Management Command-Philadelphia field survey, which starts the purchasing system review, will begin April 1, 1997.

On December 16, 1996, the Defense Supply Service-Washington provided a memorandum (see Appendix C) in response to our preliminary audit results, stating that it will:

- o emphasize the importance of approved contractor purchasing systems as a control to ensure price reasonableness on large contracts with its contracting officers;

- o direct all contracting officers to document the approval of purchasing systems during preaward survey efforts; and

- o require internal review staff to verify and document all purchasing systems with the Defense Contract Management Command in all scheduled reviews over the next 6 months.

On August 15, 1996, the Defense Supply Service-Washington provided the Defense Contract Management Command with certificates of acceptance on 19 delivery orders, extended final delivery dates on 27 delivery orders, and canceled 1 delivery order to contract MDA903-91-D-0061. The Defense Supply Service-Washington stated in its December 16, 1996, memorandum, that it will also:

- o send the Defense Contract Management Command by March 17, 1997, the status on all delivery orders identified in the June 10, 1996, request; and

- o annotate active delivery orders with the current completion date.

We consider management's completed and planned actions to be appropriate and, accordingly, make no recommendations.

Management Comments and Audit Response

Management Comments. Defense Supply Service-Washington managers provided oral comments on the draft report. The managers agreed with the thrust of the report, but believed that the draft report was inaccurate as to the frequency of and consent to subcontracting proposals. Management stated that we did not have complete documentation regarding subcontracting requests and consents, that those documents were stored separately from the primary contract files, and that we had not specifically requested that information. Accordingly, the draft report did not accurately show that the procuring contracting officer provided consent to subcontract more than the 3 of 116 contract actions cited in the draft report. Also, management disagreed that related management controls were materially weak. While acknowledging management control problems related to contract MDA903-91-D-0061, the Defense Supply Service-Washington believed that the limited scope of our audit should preclude our conclusions as to the pervasiveness or materiality of management control weaknesses.

Audit Response. We examined the additional information and further discussed subcontracting request and consent procedures with the present and former procuring contracting officers. We verified additional subcontracting

requests and related consents, but could not definitively tie each of those additional requests and consents to a particular contracting action. The requests to subcontract and the associated sole-source justifications were usually made only upon the first use of a subcontractor. Subsequent use of a particular subcontractor was seldom requested or sole-source justified, although some subcontractors were used on several contract actions. The contracting officers did not require subcontracting requests beyond the first use of a particular subcontractor, because the contracting officers believed that repeated subcontracting requests and consents for the same subcontractor was unnecessary and administratively burdensome. While such a process may be burdensome, we believe that it is necessary to meet the requirements and intent of the Federal Acquisition Regulation for sole-source subcontracting.

Because of poor documentation, we could not quantify how many of the contract actions in our sample were supported with subcontracting requests and consents. However, we still believe that few of the 116 contract actions were adequately supported, and we revised the report to so state. Also, upon reconsideration, we agree with Defense Supply Service-Washington comments that our audit of a single contract does not provide sufficient basis for determining the materiality of a management control weakness, and we revised the report accordingly.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

Contract MDA903-91-D-0061. As a result of concerns expressed by a complainant, we reviewed the management and administration of contract MDA903-91-D-0061 with Systems Research Applications Corporation. Specifically, we examined documentation, dated from May 1990 through November 1996, related to the initial award, delivery orders, and contract modifications.

Contract Management and Administration. We reviewed policy and guidance on contract management and administration in the Federal Acquisition Regulation. We interviewed personnel who provided contract management from the Office of the Assistant Secretary of Defense (Health Affairs) and the Defense Supply Service-Washington. We also interviewed personnel from the Defense Contract Management Command and the Defense Contract Audit Agency that provided contract administration and oversight. Specifically, we compared Office of the Assistant Secretary of Defense (Health Affairs); Defense Contract Management Command; and Defense Supply Service-Washington procedures for managing and administering contract MDA903-91-D-0061 to the policy in the Federal Acquisition Regulation.

Use of Computer-Processed Data and Statistical Sampling. We used computer-processed data in analyzing financial data relating to payment of delivery order invoices for contract MDA903-91-D-0061 with the Systems Research Applications Corporation. We did not establish reliability of the data because our scope was limited. However, not establishing the reliability of the data base did not materially affect the results of our audit.

We judgmentally selected 23 delivery orders for our analysis (see Appendix B). The delivery orders, dated from September 25, 1991, through July 15, 1996, were selected primarily based on their high dollar values and number of modifications. We did not project the results of our analyses of the 23 delivery orders to the universe of delivery orders.

Audit Period, Standards, and Location. We performed this program audit from July through December 1996 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary.

Audit Contacts. We visited or contacted individuals and organizations within the DoD and the Systems Research Applications Corporation. Further details are available on request.

Management Control Program

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, requires DoD organizations to implement a comprehensive system of management controls that provide reasonable assurance that programs are operating as intended and to evaluate the adequacy of controls.

Scope of Review of the Management Control Program. We reviewed the adequacy of Defense Supply Service-Washington management controls over the management and administration of contract MDA903-91-D-0061 awarded to the Systems Research Applications Corporation. Specifically, we reviewed Defense Supply Service-Washington management controls over the types of services contracted, subcontracting activities, funding of contract services, and contract closeout procedures of the contract. We also reviewed management's self-evaluation applicable to those controls.

Adequacy of Management Controls. Defense Supply Service-Washington management controls for the management and administration of contract MDA903-91-D-0061 were not adequate to ensure that subcontractors were selected through competitive procedures or that sole-source acquisitions were justified and that the prime contractor had an approved purchasing system. Because the scope of our audit was limited to a single contract, we were unable to determine whether the Defense Supply Service-Washington management control weakness was material. However, actions initiated by management (Appendix C), when implemented, should correct the weakness and improve Defense Supply Service-Washington contract procedures on other active and future contracts.

Adequacy of Management's Self-Evaluation. Defense Supply Service-Washington officials identified contract management and administration as part of an assessable unit. However, in its evaluation, Defense Supply Service-Washington officials did not identify the specific management control weakness identified by the audit because the Defense Supply Service-Washington evaluation was too broad to specifically cover whether written consent to subcontract was provided in the absence of an approved purchasing system.

Summary of Prior Audits and Other Reviews

There has been no prior audit coverage of contract MDA903-91-D-0061 within the last 5 years. However, we identified a prior review related to Defense Supply Service-Washington contract closeout practices. Inspector General, DoD, Report No. 93-INS-01, "Defense Supply Service-Washington Inspection Report," December 16, 1992, states that the Defense Supply Service-Washington had not developed a mechanism to manage and process the backlog of contract closeouts. Further, the report recommended that a plan be developed to identify and eliminate the backlog of contracts, that the plan include specific goals, and that procedures be established to monitor and track

Appendix A. Audit Process

progress. Management agreed with the report and associated recommendations. However, for contract MDA903-91-D-0061, the procedures established have not resulted in the timely closure of completed delivery orders.

Appendix B. Delivery Orders Selected for Judgment Sample

| <u>Delivery Order</u> | <u>Contract Actions¹</u> | <u>Order Date</u> | <u>Amount</u> | <u>Customer</u> |
|-----------------------|-------------------------------------|-------------------|----------------------|-----------------------------|
| 0001 | 19 | Sept. 25, 1991 | \$ 6,071,339 | Health Affairs ² |
| 0005 | 13 | Sept. 26, 1991 | 18,161,842 | Health Affairs ² |
| 0006 | 3 | Sept. 27, 1991 | 4,905,457 | Health Affairs ² |
| 0007 | 13 | Mar. 18, 1992 | 50,092,473 | Health Affairs ² |
| 0019 | 9 | Apr. 2, 1994 | 12,485,607 | USD(A&T) ³ |
| 0020 | 3 | Apr. 2, 1994 | 5,100,110 | Air Force |
| 0030 | 7 | Apr. 16, 1994 | 3,248,742 | Health Affairs ² |
| 0040 | 5 | May 27, 1994 | 1,038,856 | DFAS ⁴ |
| 0046 | 27 | June 9, 1994 | 9,771,357 | Health Affairs ² |
| 0048 | 1 | June 28, 1994 | 659,979 | Health Affairs ² |
| 0058 | 1 | Aug. 30, 1994 | 799,961 | Air Force |
| 0073 | 1 | Sept. 27, 1994 | 1,369,997 | Health Affairs ² |
| 0076 | 1 | Sept. 29, 1994 | 1,499,424 | USD(A&T) ³ |
| 0090 | 1 | Apr. 7, 1995 | 618,189 | Health Affairs ² |
| 0146 | 2 | Sept. 14, 1995 | 1,610,963 | Navy |
| 0180 | 1 | Sept. 26, 1995 | 1,249,996 | Air Force |
| 0186 | 2 | Sept. 26, 1995 | 737,565 | DUSD(AR) ⁵ |
| 0189 | 1 | Sept. 27, 1995 | 689,960 | Health Affairs ² |
| 0200 | 1 | Jan. 30, 1996 | 599,980 | Health Affairs ² |
| 0214 | 2 | Apr. 4, 1996 | 929,295 | Health Affairs ² |
| 0216 | 1 | Apr. 4, 1996 | 733,481 | Health Affairs ² |
| 0247 | 1 | July 15, 1996 | 540,000 | Health Affairs ² |
| 0248 | <u>1</u> | July 15, 1996 | <u>537,971</u> | Health Affairs ² |
| Total | 116 | | \$123,452,544 | |

¹Includes the delivery order and nonadministrative delivery order modifications.

²Assistant Secretary of Defense (Health Affairs).

³Under Secretary of Defense (Acquisition and Technology).

⁴Defense Finance and Accounting Service.

⁵Deputy Under Secretary of Defense (Acquisition Reform).

Appendix C. December 16, 1996, Memorandum on Corrective Actions Initiated



DEPARTMENT OF THE ARMY
DEFENSE SUPPLY SERVICE WASHINGTON
5200 ARMY PENTAGON
WASHINGTON DC 20310-5200

16 Dec 96

REPLY TO
ATTENTION OF
JDSSW-2A

MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL, DIRECTOR,
READINESS AND OPERATIONAL SUPPORT

SUBJECT: Results of the Audit of the Management and
Administration of Contract MDA903-91-C-0061

I have discussed with my staff the concerns you outlined, during our December 10, 1996 meeting, on subcontracting management and contract administration under the subject contract. We agree that the fact that Systems Research Corporation does not currently have an approved purchasing system is a possible contract management weakness and that more emphasis needs to be placed on the closeout of delivery orders of this contract.

The Defense Supply Service-Washington (DSS-W) will immediately draft and transmit a memorandum to all contracting officers emphasizing the importance of ensuring that contractors requiring approval of their purchasing system by regulation either have, or take steps to obtain, approval. Contracting officers will be reminded to continue to document this, as required, in the business clearance memorandum. Additionally, DSS-W will make this a special interest item during reviews conducted in the next six months by the Oversight Division, and will document the results of their reviews accordingly. Corrective action will be recommended as needed.

Concerning the closeout of delivery orders, DSS-W will notify the Defense Contract Management Command (DCMC) in writing by March 17, 1997 of the status of all delivery orders identified in the DCMC request dated June 10, 1996. The written notification will include whether the delivery order is active or should be closed out. Active delivery orders will be annotated with the current completion date.

We believe the above corrective actions address and will resolve the issues you have identified.

L. J. Stewart
Colonel, U. S. Army
Commander

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House Committee on Government Reform and Oversight
House Subcommittee on National Security, International Affairs, and Criminal
Justice, Committee on Government Reform and Oversight
House Committee on National Security

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